ROYAL TRUST NOMINEES LTD.

v.

SRI HARTAMAS DEVELOPMENT SDN. BHD.

HIGH COURT MALAYA, KUALA LUMPUR
VC GEORGE J
[ORIGINATING SUMMONS NO. D3-31-149-87]
14 JANUARY 1989

COMPANY LAW: *Loan - Ordinary shares as security - Default of terms - Transfer of shares to nominee - Did not approve or refusal to transfer - Power of veto by the Board - Exercisable within specified time - Exception, special circumstances - Rectification to effect transfer - Section 105(1) Companies Act 1965 - Damages.*

Royal Trust Merchant Bank Ltd. (lending company) has granted a loan to Asquare Credit Leasing Sdn. Bhd. (borrower) at the request of Chong Kok Lim & Sons (Holdings) Sdn. Bhd. who as security for the loan has deposited with the lending company its 2,035,000 ordinary shares of one ringgit each in a company called Sri-Hartamas Development Sdn. Bhd. by way of a charge pursuant to which the relevant memoranda of transfer duly executed by Chong Kok Lim & Sons (Holdings) Sdn. Bhd. as transferor and with the space for the name of the transferee left blank was handed to the lending company.

Upon the borrower being in default of terms of lending, the lending company decided to have the deposited shares transferred to its nominee Royal Trust Nominees Ltd. Pursuant to that decision the solicitors for the lending company on 7 January 1987 lodged with the Registrar of Sri-Hartamas Development Sdn. Bhd. the shares with the relevant memoranda of transfer duly complete with the name of nominee as transferee.

On 26 February 1987, the company secretary on behalf of Sri Hartamas Development Sdn. Bhd. wrote to the solicitors of the lending company that "we are unable to register the above transfer as the board of directors has not approved the said transfer ..."

On 27 May 1987 the transferee as plaintiff took out the instant originating summons against Sri Hartamas Development Sdn. Bhd. as defendant seeking a rectification of the defendant's register of members by entering the name of the plaintiff as holder of the shares in place of Chong Kok Lim & Sons (Holding) Sdn. Bhd. The plaintiff also seek consequential orders including damages for refusal to register the plaintiff as shareholders of the shares.

Held:

[1] Under s. 105(1) of the Companies Act 1965 and Art. 23 of the article of association of the company based on the section provide for a power of veto by the board in respect of the basic right of alienation. To be effective such veto must be exercised by positive resolution of the board and to the exercised within the prescribed period which is within a reasonable time after the lodgment of the memorandum of transfer, i.e. one month. However, the period for exercising the right of veto can be extended provided there are special circumstances.

[2] There is no special circumstances in this case and the Court cannot but conclude that on a balance of probabilities there had been no positive exercise of the veto and that what had happened was that the board had simply failed to approve the transfer.

[3] Even if in fact the board had positively exercised the veto powers they have allowed themselves to be influenced by irrelevant considerations.

[4] There will be an order as prayed in the originating summons.

[Order accordingly.]

Cases referred to:
Ho Shee Jan v. Stephens Properties Sdn. Bhd. [1986] 2 MLJ 43
Brooke v. Garrod 3 K & J 608; 2 De G & J 62
David Hey v. New Kok Ann Realty Sdn. Bhd. [1985] 1 MLJ 167
Re Avard, decd. Hook v. Parker [1948] 1 Ch 43

Legislation referred to :
Companies Act 1965, ss. 105, (1)
Evidence Act 1950, s. 114illus.(g)

For the plaintiff - Robert Lazar; M/s. Shearn Delamore & Co.
For the defendant - Chua Mei Lin; M/s. Weng Kwai & Zaid

JUDGMENT

VC George J:

Royal Trust Merchant Bank Ltd. formerly known as Arbuthnot Latham Asia Limited had granted a loan to Asquare Credit & Leasing Sdn. Bhd. at the request of Chong Kok Lim & Sons (Holdings) Sdn. Bhd. who as security for the loan deposited with the lending company its 2,035,000 ordinary shares of one ringgit each in a company called Sri Hartamas Development Sdn. Bhd. by way of a charge pursuant to which the relevant memoranda of transfer duly executed by Chong Kok Lim & Sons (Holdings) Sdn. Bhd. as transferor and with the space for the name of the transferee left blank was also handed to the lending company.

Upon the borrower being in default of terms of the lending, the lending company decided to have the deposited shares transferred to its nominee Royal Trust Nominees Ltd. Pursuant to that decision the solicitors for the lending company on 7 January 1987 lodged with the Registrar of Sri Hartamas Development Sdn. Bhd. the shares with the relevant memoranda of transfer duly completed with the name of the said nominee as transferee.

By a letter dated 4 February 1987 the company secretary of Sri Hartamas Development Sdn. Bhd. informed the said solicitors *vis-a-vis* the registration of the transfer of the shares "our board of directors have been unable to meet to consider (the matter) in view of the long Chinese new year holiday season."

By a letter dated 23 February 1987 the said solicitors wrote to Sri Hartamas Development Sdn. Bhd., and referred to the said letter of 4 February 1987 in enquiring what would be "the date for requisite board meeting to be held to give effect to the transfer." In reply the company secretary on behalf of Sri Hartamas Development Sdn. Bhd. wrote to the said solicitors her letter of 26 February 1987:

> We write to inform you that we are unable to register the above transfer as the board of directors has not approved the said transfer at its meeting held on 25 February 1987. Accordingly, we return herewith the following documents...

On 27 May 1987 the transferee as plaintiff took out the instant originating summons against Sri Hartamas Development Sdn. Bhd. as defendant seeking a rectification of the defendant's register of members by entering the name of the plaintiff as holder of the shares in place of Chong Kok Lim & Sons (Holdings) Sdn. Bhd. and for consequential orders including an order that the defendants pay damages to be assessed for the refusal to register the plaintiff as shareholder of the shares. The application was supported by the affidavit of En. Rahmat

Jamari the solicitor in the plaintiff's solicitors' firm who had the conduct of the matter. He exhibited to his affidavit copies of the said correspondence between the said solicitors and Sri Hartamas Development Sdn. Bhd. The affidavit of Francis Lee the manager of the lending company affirmed on 12 June 1987 was also filed in support. Mr. Lee in his affidavit stated *inter alia* that he had been advised and verily believed "that the defendant has not to date refused to register the transfer as evidenced in Exhibit RJ14 to the affidavit of Rahmat Jamari." RJ14 is the said letter of Sri Hartamas Development Sdn. Bhd. dated 26 February 1987 and what the plaintiffs would, it seems, highlight in the letter is that the company secretary wrote that "the board of directors has not approved the transfer at its meeting held on 25 February 1987".

Section 105 of the Companies Act makes it mandatory that if a company refuses to register a transfer of shares it shall, within one month after the date on which the transfer was lodged with it, send to the transferor and transferee notice of the refusal.

Article 23 of the articles of association of the company consistent with s. 105 provides as follows:

> 23. The directors may, in their discretion, and without assigning any reason therefore, refuse to register a transfer of any share to any person of whom they do not approve, and they may also refuse to register a transfer of any share on which the company has a lien. If the directors refuse to register a transfer they shall within one month after the date on which the transfer was lodged with the company send to the transferee notice of the refusal in accordance with s. 105 of the Act.

For the plaintiffs Francis Lee further contends in his affidavit that if in fact the veto power reserved to the directors had been exercised it was exercised outside the prescribed time limit and as such was ineffectual. In any event, it was contended the power was not exercised *bona fide* in the interest of the defendants but in the interest of the Chong Kok Lim family (who it was suggested control the chargor company and perhaps the borrower company as well as Sri Hartamas).

The originating summons together with the affidavits of Rahmat Jamari and Francis Lee were served on the defendant company on 22 June 1987.

It was a member of the Chong Kok Lim family who affirmed the affidavit on 11 November 1987 that was read in opposition to the application. He is Mr. Chong Wai Hiong. He was one of the four directors of Sri Hartamas Development Sdn. Bhd. The other there being his father Tan Sri Chong Kok Lim, his brother Chong You Hiong and one Dato Wong Kee Tat.

Inter alia Mr. Chong Wai Hiong contends by his affidavit that at the board meeting of 25 February 1987 it was resolved that the request to register the shares be rejected and that the secretary be instructed to inform the plaintiff of the board of directors' decision. He went on to state in para. 7 of his affidavit:

> 7. Thus the plaintiff was informed by way of a letter dated 26 February 1987 that the defendant was unable to register the transfer as the board of directors had rejected the said request for transfer at its meeting held on 25 February 1987.

As confirmation of what took place at the board meeting what was purported to be an extract of the relevant directors' resolution was exhibited (certified as true by the secretary) as Exhibit CWH2 to Chong Wai Hiong's affidavit. This extract is dated 22 June 1987 which it is to be noted is the day on which the originating summons and the accompanying affidavit were served on Sri Hartamas Development Sdn. Bhd.

I pause to look again at the company secretary's letter of 26 February 1987 and note that contrary to what is stated in the said para. 7 of Chong Wai Hiong's affidavit, in fact the plaintiffs were informed through the said letter to its solicitors that the defendant was unable to register the transfers as the board of directors had not approved the said transfer. The letter does not state that the application had been rejected.

It seems to me that clearly there is an inconsistency between the reasons given for the defendant not being able to register the transfer as set out on the one hand in the company secretary's letter of 26 February 1987 and on the other in the extract from the minutes of the board meeting and in the said para. 7 of Chong Wai Hiong's affidavit.

The company secretary did not come forward with an affidavit or other-wise to explain the inconsistency. No doubt Mr. Chong Wai Hiong when cross-examined on the inconsistency refused to accept that there was an inconsistency. He expressed the opinion that "had rejected" and "has not approved" amounted to the same thing. I do not for a moment think that the defendant's legal advisers laboured under any such misapprehension. Accordingly I would have expected the defendant to have had the company secretary come forward by affidavit or otherwise to explain the inconsistency and to produce the original minutes of the board meeting. In the context the omission to do so and in particular the omission to produce the minute book of the company displaying the original minutes as recorded at the meeting acquires significance as does the fact that the extract purported to be of the board resolution was made on 22 June 1987 the very date on which the defendant was served with the affidavit of Francis Lee.

The effect of s. 105 of the Companies Act has been discussed at length by N.H. Chan J in *Ho Shee Jan v. Steptens Properties Sdn. Bhd.* [1986] 2 MLJ 43 where he analysed the leading English judgments on the effect of the equivalent section in the English Act. What is shown to have been established and which I respectfully accept as being the law on the point is that a share in a company is freely alienable property. However s. 105 of the Companies Act 1965 and articles in the articles of association of a company based on that section provide a power of veto by the board in respect of this basis right of alienation. To be effective such veto must be exercised by a positive resolution of the board. If limitations are built into the power of veto the board has to restrict the exercise of the power of veto within the terms of the restrictions. The power of veto has to be exercised within the prescribed period which is within a reasonable time after lodgment of the memorandum of transfer and in any event (in England) not later than two months after such lodgment because the relevant English section provides two months within which the transferee and transferor have to be notified of the exercise of the veto. In Malaysia our s. 105 is in *pari materia* with the English section but provides only one month within which the transferor and the transferee have to be notified of the exercise of the veto and it follows a *fortiorari* that the outside time limit in Malaysia for the exercise of the option is one month from the date of lodgment of the memorandum of transfer. In my judgment the effect of s. 105 of the Companies Act 1965 and Art. 23 of the articles of association in the instant case is that the company reserves to its directors an option which if they do not exercise within the prescribed period ceases to be available to them. In *Brooke v. Garrod* 3 K & J 608; 2 De G & J 62 (applied and quoted at length in *re Avard, decd. Hook v. Parker* [1948] 1 Ch. 43) Lord Cranworth LC said at p. 66:

> Now I have more than once had occasion to say that I think this Court has gone to too great an extent in departing from the precise terms of the contracts into which parties have entered, and so in effect making other contracts for them. If a contract can, by fair construction, be divided into two contracts, i.e. one contract to do an act and another to it at a certain time, the Court may say that these are independent stipulations. But if the contract be that

> on payment of a sum of 1,000 pounds at or before a specified day, a certain act shall be done on my part, I am at a loss to see why I can properly be called on to do the act if the money be not paid at the day; or why I should be compelled to perform not my contract but another contract into which I have not entered. If cases are found in the books, which go to that extent, I can only say that I cannot see the principle on which they are founded... There may be a distinction where a person, being ready and willing to comply with a condition, has been prevented from so doing. That raises a question of a different class, and I should be loath to say that the Court would not find the means of giving relief if the donee had done all that in him lay, and if the delay was to be attributed to the other contracting party. (This passage is quoted in *re Avard* at p. 47.)

The rule in *David Hey v. New Kok Ann Realty Sdn. Bhd.* [1985] 1 MLJ 167 is an exception to the general rule that the right of veto has to be exercised within the time constraints. In my judgment the effect of David Hey is that the period for exercising the option can be extended provided there are special circumstances. The special circumstances accepted in that case were that the share register, minute book and other documents of the company were not available to the board to enable them to give due consideration to the application to transfer the shares within the prescribed period. No doubt some mention was also made in the judgment of the fact that the guidelines for the regulation of acquisition of assets, mergers and take-overs issued by the government in 1974 have not been complied with. Non-compliance of the regulations no doubt can afford the directors a *bona fide* ground for exercising the veto. But such non-compliance does not permit any extension of the time to exercise the veto. The rule in *David Hey vis-a-vis* the extension of the prescribed time within which the veto should be exercised in effect is that the special circumstances should amount to a situation that makes it virtually impossible for the board to have properly directed their minds to the issue of exercising the veto. It seems to me there should be no difficulty in accepting that ratio when one starts off with accepting that the shares of the company is an item of property freely alienable and if restrictions are made on this right then there must be a strict application of the powers reserved to the board. Company secretaries and Registrar of Companies and boards of directors of companies should be deemed to know the terms of the contract between the company and its members and under which the company functions namely the memorandum and articles of association and if rights and power reserved thereby are not exercised in due time the right to exercise them will be deemed to have ceased to be available. It follows that whether the delay is 19 days or 4 months is irrelevant.

Are there special circumstances here? I think not. The evidence is that if they wanted the members of the board could have met on the date first reserved for the hearing of the application, namely 26 January 1987. The excuses given for not having held the meeting do not, in my judgment, amount to special circumstances, certainly not in the face of the statutory time limit of one month.

The other question that arises is whether there had in fact been a positive resolution of the board whereby the power of veto was exercised. Having been challenged as they were on this point, the challenge being supported by the company secretary's letter to the applicant's solicitors which, on the face of it, suggests that there had been no positive resolution by way of the exercise of the power of veto, the burden of proving that in fact there had been such positive exercise of the power falls on the company which, in my judgment, they have failed to discharge. To rely on an extract of the minutes which on the face of it was inconsistent with the letter of 26 February 1987 without exhibiting the original minutes with no explanation for the omission calls for an invocation of the presumption under s. 114(g) of

the Evidence Act. In the event the Court cannot but conclude that on a balance of probabilities there had been no positive exercise of the veto and what had happened was that the board had simply failed to approve the transfer.

Finally I am also of the opinion based on the evidence of Mr. Chong Wai Hiong that if in fact the board had positively exercised the veto powers they have allowed themselves to be influenced by irrelevant considerations, namely, the taking into account of a pre-emption provision when in fact there was no such pre-emption clause in the articles. In his testimony Mr. Chong said that there was a verbal understanding among the three groups that own the company that shares of the company must be offered to the others of them first and only if the offer was rejected would the transfer to a third party be considered.

There will be an order in terms of prayers 1, 2, 3 and 4 of the originating summons.

Also found at [1989] 2 CLJ 1069